

In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. See 86 Ill. Adm. Code 130.1940. (This is a GIL.)

January 12, 1999

Dear Ms. Xxxxx:

This letter is in response to your letter dated June 16, 1998. We regret the delay in our response. The nature of your letter and the information you have provided require that we respond with a General Information Letter which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

We are an electrical contractor for the repair and installation of industrial machinery. According to the state of STATE, where we are located, we are required to pay sales tax on anything we purchase in connection with our contract and then we do not collect sales tax from our STATE customers. Since we pay sales tax in this manner, on jobs we will be contracting to customers in your state, are we obligated to in turn collect sales tax from our customer in your state? And, if so, what exactly is the tax based on. Please send us your official ruling on this, as well as your general documentation at your earliest convenience.

Since you describe yourself as an electrical contractor, we are assuming that you are a contractor within our definition. Please find enclosed copies of 86 Ill. Adm. Code 130.1940 and 130.2075 regarding the tax liabilities of contractors in Illinois. The term construction contractors includes general contractors, subcontractors, and specialized contractors such as landscape contractors. The term contractor means any person or persons who are engaged in the occupation of entering into and performing construction contracts for owners. In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. As end users of such tangible personal property, contractors incur Use Tax liability for such purchases based upon the cost price of the tangible personal property. Therefore, any tangible personal property that general contractors or subcontractors purchase that will be permanently affixed to or incorporated into real property in this State will be subject to Use Tax. If contractors did not pay the Use Tax liability to their suppliers, contractors must self-assess their Use Tax liability and pay it directly to the Department.

As previously stated, contractors are deemed end users of property that is purchased for incorporation into real property. If general contractors did not purchase the tangible personal property, then the general contractors cannot be

held liable for tax due on another entities' purchases. If subcontractors are utilized and are acting as construction contractors, the transaction between the general contractors and the subcontractors is not a taxable transaction. The subcontractors incur Use Tax liability on any tangible personal property that they purchase for incorporation into real estate. If, however, general contractors make purchases and then contract to have subcontractors do the installation, the general contractors incur Use Tax liability because they are making the purchases of such tangible personal property.

In Illinois, organizations that are determined by the Department to be exclusively charitable, religious, educational, or a governmental body, are issued tax exemption identification numbers ("E" numbers). Organizations holding such numbers are exempted from paying sales tax on organizational purchases. The organization must obtain and present this number to a retailer, however, before it can make a tax-free purchase. Suppliers selling tangible personal property to such exempt organizations must retain the "E" number in order to document the exempt sale.

As stated above, contractors are generally considered to be the end users of tangible personal property they permanently incorporate into real estate and owe Use Tax upon their purchases. However, contractors who physically incorporate tangible personal property into real estate owned by holders of "E" numbers can purchase such property tax-free by providing their suppliers with the certification described in Section 130.2075(d), as well as the "E" number of the group into whose real estate that property will be incorporated. The suppliers should retain this information in order to document the tax-exempt sale.

Sales of tangible personal property to a construction contractor who does not incorporate the items into real estate owned by an exempt organization are subject to tax. Items which are purchased tax-free because of their intended incorporation into real estate owned by an exempt organization, but which are not, in fact, incorporated into real estate owned by an exempt organization, are also subject to tax.

Construction contractors incur Retailers' Occupation Tax liability when they engage in selling any kind of tangible personal property to purchasers without permanently affixing the tangible personal property to real estate. See 86 Ill. Adm. Code 130.1940(b)(1). Construction contractors can purchase such tangible personal property tax-free for resale by providing their suppliers with Certificates of Resale. See 86 Ill. Adm. Code 130.1405, enclosed. Their Illinois suppliers and suppliers who are "retailers maintaining a place of business in Illinois" (see discussion below), must retain certificates of resale in order to document the resale exemption.

The basic State rate of tax under the Retailers' Occupation Tax Act is 6.25%. In addition to the basic State rate of tax, depending upon the selling location of the retailers, there may be local taxes that apply in addition to the basic State rate of tax. The basic State rate of tax under the Use Tax Act is 6.25%.

As stated above, construction contractors who sell tangible personal property must either pay tax or document an exemption. The manufacturing

machinery and equipment exemption from sales tax is available for sales of machinery and equipment used primarily in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease. See the Department's rules for this exemption set forth at 86 Ill. Adm. Code 130.330, copy enclosed. The process must meet the requirements of manufacturing or assembling set forth in the Department's rules. In addition, the machinery or equipment must be used primarily (over 50% of the time) in a qualifying manufacturing or assembling process. Exemption certificates must be executed by the purchaser and submitted to the retailer. Form ST-587, Machinery and Equipment Exemption Certificate, may be used to document the manufacturing machinery and equipment exemption.

The equipment must also meet the requirements of machinery or equipment set forth in the Department's rules. Please note that Section 130.330(d)(4)(H) provides that "[t]he use of machinery or equipment for general ventilation, heating, cooling, climate control or general illumination, not required by the manufacturing process" will generally not be considered to be manufacturing. Machinery and equipment of this type would only qualify if required by the manufacturing process.

In the context of sales to contractors who will incorporate qualifying machinery and equipment into real estate as part of a construction contract, purchasing contractors should provide their sellers with certifications that the machinery will be transferred to a manufacturer as manufacturing equipment in the performance of a construction contract for that manufacturer. Purchasing contractors should include the manufacturer's name and registration number to claim the exemption.

Whether or not companies incur tax liability depends on whether they establish nexus with Illinois. Illinois retailers are ones who either accept purchase orders in the State of Illinois or maintain an inventory in Illinois and fill Illinois orders from that inventory. The Illinois retailers are liable for Retailers' Occupation Tax on gross receipts from sales and must collect the corresponding Use Tax incurred by purchasers. Generally, contractors who perform work in Illinois are considered to have nexus with the State.

If machinery permanently affixed to real estate is repaired, construction contractors owe Use Tax on items they transfer. However, in regards to repairing machinery that is not permanently affixed to real estate, please note that Retailers' Occupation Tax and Use Tax do not apply to receipts from sales of personal services. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. For your general information we are enclosing a copy of 86 Ill. Adm. Code 140.101 regarding sales of service and Service Occupation Tax.

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or, (4) Use Tax on cost price if the servicemen are de minimis and

are not otherwise required to be registered under the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See, 86 Ill. Adm. Code 140.101(f) enclosed. This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self-assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers, nor are they liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis.

Regarding issues of multi-state taxation, please be advised that the Illinois Use Tax Act contains provisions that limit multi-state taxation of the same item or items. As the enclosed copy of 86 Ill. Adm. Code 150.310 explains, a purchaser using tangible personal property in Illinois which has been purchased outside of Illinois and who has paid a tax in another state in respect to the sale, purchase, or use of that property is entitled to a credit, to the extent of the tax properly due and paid in the other state, against this Illinois Use Tax liability.

I hope this information is helpful. The Department of Revenue maintains a Web site which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.